

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
HALUK INCE	:	DETERMINATION
	:	DTA NO. 818537
for Revision of a Determination or for Refund of Sales	:	
and Use Taxes under Articles 28 and 29 of the Tax Law	:	
for the Period February 1, 1997 through May 31, 1999.	:	

Petitioner, Haluk Ince, 98 Knapp Avenue, Rochester, New York 14609-1128, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period February 1, 1997 through May 31, 1999.

A hearing was held before Gary R. Palmer, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on February 22, 2002 at 10:30 A.M., with all briefs to be submitted by September 16, 2002, which date began the six-month period for the issuance of this determination. Petitioner appeared by Erdal Erol, Enrolled Agent. The Division of Taxation appeared by Barbara G. Billet, Esq. (Clifford M. Peterson, Esq., of counsel).

ISSUES

I. Whether the indirect audit method employed by the Division of Taxation was reasonably calculated to determine sales tax due.

II. Whether the Notice of Determination issued to petitioner was sufficiently free of material defects so as to give rise to a valid assessment of sales tax due.

FINDINGS OF FACT

1. During the period at issue petitioner was a shareholder and an officer of Ozay-Ince, Inc. d/b/a Dick's Automotive ("the corporation"), which conducted business at 1125 Titus Avenue, Rochester, New York.

2. The corporation, during the period at issue, was engaged in the retail sale of gasoline, cigarettes, used cars, automotive repairs and related merchandise that included motor oil and windshield washer fluid.

3. Petitioner, in addition to being an officer and part owner of the corporation, was engaged in the day-to-day operation of the business of the corporation, had corporate check signing authority and signed sales tax returns, New York State motor vehicle retail certificates of sale (Form MV-50), New York State cigarette and tobacco product retail dealers applications (Form ST-134), corporate checks and the corporation's New York State sales tax registration.

4. On May 3, 1999 the auditor for the Division of Taxation ("the Division"), Mr. Dunleavy, called petitioner and informed him that he, the auditor, wanted to schedule an appointment for a sales tax audit. Petitioner referred the auditor to his representative, Mr. Erol. On May 4, 1999 the auditor called Mr. Erol, who agreed to meet with the auditor at the business location on May 10, 1999 to commence the audit. Mr. Dunleavy confirmed the conversation in his letter dated May 5, 1999 to Mr. Erol, which letter specifically requested the production of all documents pertinent to the preparation of the corporation's tax returns, and directed the representative's attention to an enclosed power of attorney form and an attached list of records to be produced at the audit for the entire audit period. The letter identified the audit period as "3/1/96 - present." The attached list of records to be produced included the following:

sales tax returns and related schedules, bulk receipts and invoices from suppliers, fuel disbursements (sales and self use), exemption certificates, cash register tapes, product lists, capital asset list and related invoices, federal tax returns (1120s), service station records and FT-943 service station reports.

5. On May 10, 1999 the auditor and his supervisor, Mr. Smigielski, went to the business location and met with petitioner who gave the auditors a tour of the business and an explanation of the product line sold. Mr. Erol arrived an hour late because he was not feeling well. No records were supplied to the Division on May 10. A new appointment was agreed to later the same week at Mr. Erol's office, which appointment was later changed to May 25, 1999. On May 25, the auditor and his supervisor met with Mr. Erol and petitioner at Mr. Erol's office for the initial conference. Copies of the corporation's sales tax returns with attached handwritten notes and documents relating to unrelated "L" assessments were furnished by the corporation at this meeting. No other records were received during the course of the audit. By letter dated May 27, 1999 to Mr. Erol, with a copy to petitioner, the auditor acknowledged receipt of the sales tax returns and restated the Division's prior records request in the body of the letter as follows:

quarterly Inventory Reports by Retail Service Stations, gasoline purchase invoices, cigarette purchase invoices, all other purchase invoices (oil, window cleaner, etc.), all sales and repair invoices (particularly auto sales invoices) and sales journals, check/cash disbursement register, cash register tapes, Federal tax returns (1120s), capital asset list and related invoices and monthly fuel inventory (stick and/or meter readings).

The auditor closed the May 27 letter with a statement to the effect that if the requested information was not received by June 17, 1999 additional tax due would be estimated.

6. By letter that was intended to be dated July 20, 1999, but which misstated the date as July 20, 1998, the auditor restated his request for the list of records specified in his May 27, 1999

letter. No further records were received in response to the July 20 letter, although the Division did receive a signed consent extending the period of limitations for the corporation.

7. At this point the auditor was coming to realize that his efforts to obtain books and records from the corporation were futile. He then proceeded to secure returns filed by the corporation's wholesale gasoline distributor with the Division, which returns reflected the gallons of gasoline the distributor sold to the corporation during the audit period.

8. The auditor computed the corporation's gasoline gallons purchased by sales tax quarter throughout the 12-quarter audit period and compared those gallons, quarter by quarter, with the reported gallons sold from the filed sales tax returns. To determine audited gallons sold for each quarter, the auditor adopted either the total gallons purchased for each quarter or the gallons reported sold for that quarter, depending on which gallonage figure was greater. By using this method the auditor arrived at total gasoline sold for the audit period of 776,390 gallons. He then multiplied the audited gallons sold for each quarter by \$1.549 per gallon, to arrive at audited taxable gasoline sales for each quarter, which for the 12 quarters in the audit period totaled \$1,202,628.12. The \$1.549 audited selling price was determined by the Division to be a fair average selling price for all three grades of gasoline sold in the Rochester-Buffalo area for the December 1999 time frame. This average was not weighted to account for any differences that might have existed in the sales volume of the three grades of gasoline sold.

9. The audited taxable fuel sales for each quarter were multiplied by the eight percent Monroe County sales tax rate to arrive at an audited sales tax figure of \$96,210.24, to which a credit for prepaid sales tax was applied. The prepaid sales tax credit was computed by multiplying the gallons purchased as determined from the gasoline distributor's records by the

Region 2 prepaid sales tax rate determined in accordance with 20 NYCRR 561.11 and 561.12. The credit for prepaid sales tax so determined for each quarter was subtracted from the audited taxable sales for each corresponding quarter leaving as total audited sales tax due from gasoline sales for the 12 quarters of the audit period the sum of \$47,199.27.

10. To determine used car sales, auto repair sales, cigarette sales and miscellaneous automotive product sales, the auditor relied on his office's experience in auditing a similar business in the Rochester area that sold, in addition to gasoline, the same general product line as the corporation. With regard to the auditor's office experience with this other unnamed entity that also sold used cars, it was determined that the entity sold 41 cars per quarter at an average selling price of \$8,900.00. For petitioner's corporation the auditor assumed that it sold one car per week at an average selling price of \$5,000.00 or \$65,000.00 per quarter and \$780,000.00 for the 12-quarter audit period.

11. As to cigarette sales, the auditor's office experience with this unnamed entity included a determination that it sold 2,170 packs of cigarettes per quarter, which was consistent with the quarterly cigarette sales of approximately 18 other Rochester area gasoline station audits that the audit supervisor had experience with over the course of the previous two years. Based on this office experience, the auditor assumed that petitioner's corporation sold 2,170 packs of cigarettes per quarter at \$2.75 per pack for the first four quarters, \$3.00 per pack for the next four quarters, and \$3.50 per pack for the final four quarters of the audit period, for total cigarette sales of \$80,290.00 for the 12-quarter audit period. The prices stated per pack were equal to the New York State minimum allowable cigarette sales price. No credit was given for the prepaid sales tax on cigarettes because no cigarette purchase invoices were provided.

12. Based on the audit supervisor's experience with the same approximately 18 gasoline station audits whose sales included automotive repair work with multiple major auto repairs being performed each day, and the observation by the audit supervisor that the corporation had more than one person working in the corporation's single service bay on the day of his visit, the auditor assumed that the corporation did one major auto repair per week at an average price of \$500.00. By extrapolating the \$500.00 over the 12 quarters at \$6,500.00 per quarter, the auditor determined total taxable automotive repair sales to be \$78,000.00 for the audit period. The Division labeled the repair sales as miscellaneous sales and made no separate effort to audit sales of motor oil or windshield washer fluid that may have been sold separately from the automotive repair sales.

13. The Division determined sales tax due from the corporation for the 12 quarters at issue to be \$72,301.11 for which a notice of determination was issued to the corporation on January 20, 2000 for the tax as stated plus penalty and interest for a total of \$110,791.46. Because the Division obtained no consent agreement extending the period of limitation as to petitioner, by the time the notice of determination was issued to him on February 22, 2000, the earliest two tax quarters had expired. Petitioner's notice imposed tax, plus penalty and interest, for only the most recent 10 quarters of the 12 for which the corporation was assessed.

14. The notice of determination issued to petitioner bore the following statement in its "Explanation and Instructions" section:

This notice is issued because you are liable as an Officer/Responsible Person for a penalty in an amount equal to the tax, penalty and interest not paid by the business indicated below. (section 1145(e) of the New York State Tax Law).

Our records indicate that you are/were an Officer/Responsible Person of:
OZAY-INCE, INC.

The "Computation Summary Section" of petitioner's notice lists no sums due in the tax column or the interest column, but rather sets forth all sums due for tax, penalty and interest as a single figure in the penalty column for each of the 10 quarters open as to petitioner for a total of \$99,892.93.

15. A conciliation conference was timely requested and then held on July 24, 2000. Following the conference a meeting was held at Mr. Erol's office. At this meeting Mr. Erol produced a quantity of the corporation's cash register tapes covering the quarter from September 1, 1998 to November 30, 1998, showing sales other than gasoline. The total sales for that quarter from the cash register tapes were \$49,526.18 which were compared to the corporation's sales as reported on its sales tax return for that quarter. The reported sales totaled \$38,025.00. The auditor used this information to compute an error rate of 30.25 percent which he applied across the 12-quarter period at issue. In recomputing the tax the auditor omitted the separate computation for sales tax on cigarettes based on his belief that the cash register tapes included cigarette sales. In addition, the auditor applied to the New York State Department of Motor Vehicles for copies of the corporation's automotive retail certificates of sale (Form MV-50) for the period from December 1, 1997 through May 31, 1999. The record included 54 Forms MV-50 as well as information on retail pricing of automobiles acquired by the auditor from the Kelley Blue Book web site in December 2000. From this information the corporation's used car sales were revised downward from \$780,000.00 to \$175,885.00 for the 12-quarter audit period.

16. Audited sales tax due from gasoline sales for the 12 quarters was reduced from \$47,199.27 to \$35,797.62 by excluding New York State excise tax from the fuel sales

computation. The corporation's revised additional sales tax due was reduced from \$72,301.11 plus penalty and interest to \$46,024.10 plus penalty and interest. On January 19, 2001 a conciliation order was issued to petitioner imposing tax in the sum of \$46,024.10 plus penalty and interest. On April 20, 2001 the Division of Tax Appeals received petitioner's petition filed in protest of the conciliation order.

17. At the hearing the audit supervisor testified that the tax stated in the conciliation order issued to petitioner was in error because it was based on all 12 quarters instead of only the most recent 10 quarters that were open as to petitioner. Mr. Smigielski conceded that the correct amount of petitioner's sales tax liability should be reduced to \$39,253.45 plus penalty and interest.

SUMMARY OF THE PARTIES' POSITIONS

18. The Division asserts that it made repeated written requests of petitioner and his representative for books and records of the corporation's sales that would support a detailed audit of the corporation's sales tax liability. When such records were not produced the Division computed the corporation's sales tax liability by using third-party information showing the corporation's gasoline purchases for the audit period, and then office experience to conservatively estimate sales tax due from other segments of the corporation's product line. When, following the conciliation conference, petitioner's representative produced cash register tapes for the quarter ending November 30, 1998, the corporation's sales tax liability was revised downward.

19. Petitioner, through his representative, concedes that the corporation's record keeping, pricing and sales reporting practices were mismanaged. Mr. Erol stated that petitioner and his

co-owner sold gasoline at cost or less and other products at a very low price in order to be competitive. With regard to the audit, Mr. Erol testified that the determination of additional sales tax due was excessive because the gasoline mark-up employed by the Division was overstated. Mr. Erol did not question the Division's determination that petitioner was a responsible officer of the corporation and did not offer any evidence in support of a finding of reasonable cause for the abatement of penalty.

CONCLUSIONS OF LAW

A. When, as here, the Division resorts to an indirect audit method, it must establish that the taxpayer's books and records were so deficient as to render it virtually impossible to determine the taxpayer's liability solely from those books and records (***Matter of Urban Liquors, Inc. v State Tax Commission***, 90 AD2d 576, 456 NYS2d 138). In order to establish that the taxpayer's books and records are inadequate, the Division must first request (***Matter of Christ Cella v State Tax Commission***, 102 AD2d 352, 477 NYS2d 858) and then thoroughly examine the books and records for the entire audit period (***Matter of King Crab Restaurant v Chu***, 134 AD2d 51, 522 NYS2d 978). The record clearly supports the Division's repeated clear and unequivocal requests for source documents bearing on the corporations's sales and its failure to keep or produce such records for the Division's review. The auditor reasonably concluded and petitioner's representative conceded that the corporation's books and records were insufficient to verify its taxable sales for the audit period. Having established the insufficiency of the corporation's books and records, the Division properly resorted to external indices in the form of third-party records of the corporation's gasoline purchases and the auditor's office experience.

B. It is the Division's obligation to select an audit method that is reasonably calculated to reflect sales tax due (*see, Matter of Grant v Joseph*, 2 NY2d 196, 159 NYS2d 150, *cert denied*, 355 US 869, 2 L Ed 2d 75; *Matter of Ristorante Puglia, Ltd. v Chu*, 102 AD2d 348, 478 NYS2d 91). On the other hand, it is petitioner's burden to show that the audit method employed by the Division or the amount of tax assessed is erroneous (*Matter of Surface Line Operator's Fraternal Org. v Tully*, 85 AD2d 858, 446 NYS2d 451). Petitioner has done neither. While professing in his testimony and his brief that the estimated selling price of gasoline used by the Division in its audit was too high, petitioner's representative produced no evidence in support of his premise. Nor was there any evidence produced during the audit on petitioner's behalf that served to challenge the Division's estimates relating to used car sales, cigarette sales, or automobile repair sales. That, following the conciliation conference, the Division made adjustments in petitioner's favor upon receiving cash register tapes from petitioner for one quarter does not serve to invalidate an otherwise valid indirect audit method employed by the Division.

C. A determination of tax must have a rational basis in order to be sustained upon review (*see, Matter of Grecian Square v New York State Tax Commission*, 119 AD2d 948, 501 NYS2d 219). This rational basis arises from the presumption of correctness that, in turn, flows from the issuance of an assessment when there is no evidence introduced challenging that assessment (*Matter of Atlantic & Hudson Limited Partnership*, Tax Appeals Tribunal, January 30, 1992; *Matter of Hammerman*, Tax Appeals Tribunal, August 17, 1995; *Matter of Goldapper*, Tax Appeals Tribunal, February 7, 2002). It is petitioner's burden to produce evidence sufficient to overcome the presumption of correctness surrounding the Division's

estimates of the corporation's taxable gasoline sales, cigarette sales, automotive repair sales and used car sales. Petitioner, whose liability is derived from the corporation's sales tax liability, has not met this burden.

D. The petition of Haluk Ince is granted to the extent indicated in Finding of Fact 17 and the notice of determination is otherwise sustained.

DATED: Troy, New York
March 14, 2003

/s/ Gary R. Palmer
ADMINISTRATIVE LAW JUDGE